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C O N F I D E N T I A L SECTION 01 OF 04 MOSCOW 000301

SIPDIS

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TAGS: [EPET](#) [ENRG](#) [ECON](#) [PREL](#) [MARR](#) [PARM](#) [RS](#) [IR](#)

SUBJECT: RUSSIA MAY VIEW IRAN AS A POTENTIAL ECONOMIC
RIVAL, NOT A PARTNER

REF: A. 09 MOSCOW 3010

[1](#)B. 09 MOSCOW 3002

Classified By: Ambassador John R. Beyrle for Reasons 1.4 (b/d)

SUMMARY

[1](#)1. (C) Rhetoric from politicians and pundits aside, Russian-Iranian economic relations are relatively minor. Total two-way trade between the two countries is less than \$3 billion, or 0.6% of total Russian trade. Investment flows are similarly weak. While both sides seek to expand the economic relationship, Iran is unlikely to become a major Russian economic partner anytime soon. MFA Iran desk head Maxim Baranov told us on February 5 that concrete progress on expanding economic ties has been slow. He also noted that attempts to strengthen the bilateral banking relationship are partly driven by the difficulty, due to U.S. sanctions, of conducting trade with Iran in dollars. Iran's strategic significance for Russia may be more as a regional political and economic rival rather than as a partner. With the Russian economy largely dependent on oil and gas exports, and Russia's influence in Eurasia tied to its role as the largest energy supplier, a more stable and prosperous Iran may present more of a challenge than a benefit to Russian interests in the medium term. End summary.

RELATIVELY INSIGNIFICANT ECONOMIC RELATIONSHIP

[1](#)2. (SBU) Observers sometimes note that Russia's economic ties with Iran are an important factor in Russia's political posture toward the country. However, economic ties between the two countries are relatively insignificant for Russia. Russian exports to Iran, led by consumer goods, oil and gas equipment, and military technology, amounted to just under \$2.5 billion in the first 11 months of 2009. Russian imports from Iran in the same period were under \$200 million. While the figures were down from previous years due to the economic crisis, the relative value of the trade flows for Russia have not changed much. In 2009, two-way trade between Russia and Iran represented only 0.6% of total Russian trade volumes.

While figures for investment flows are more difficult to ascertain, bilateral direct investment appears similarly low.

The Intergovernmental Agreement on Trade and Economic Cooperation signed in 1997, as well as the Agreement on Mutual Aid in Customs, and the Agreement on Avoiding Double Taxation concluded in 2001, govern Russian-Iranian trade and economic relations.

OIL AND GAS

13. (SBU) The most obvious area of potential economic interaction between Russia and Iran would seem to be in the energy sector, but even there the results are thin, consisting mostly of intergovernmental MOUs and agreements with few, if any, tangible results. In July 2008, Gazprom and the National Iranian Oil Company (NIOC) signed an MOU on oil and gas development in Iran, including possible Gazprom participation in a planned pipeline that would deliver Iranian gas to Pakistan and India (IPI). On November 11, 2009, Gazpromneft (the oil arm of Russia's state-owned gas giant Gazprom), and the NIOC signed an MOU regarding the development of the Azar and Shargule oil fields in Iran. According to a press release by Gazpromneft, the companies will "evaluate the project's technical and economic feasibility and then move on to preparing a full-fledged contract." Other Russian firms that have expressed interest in working in Iran include Sibur Holding petrochemical company and Stroytransgaz, Gazprom's gas construction subsidiary.

MOSCOW 00000301 002 OF 004

14. (C) Gazprom is already invested in the development of Iran's South Pars gas field (ref B). However, Ivan Zolotov, Gazprom's Foreign Relations Director, recently told us that Iran is not a priority for Gazprom and expansion of Gazprom's presence has stalled. Privately owned Russian oil giant Lukoil has a minor investment in an exploration project in Iran, which a senior Lukoil executive described to us as "dormant."

15. (SBU) In October 2008, Russia and Iran joined with Qatar, in what Gazprom Chairman Alexey Miller was reported as describing as a "big gas troika," but that effort and the Gas Exporting Countries Forum (GECF), of which both Russia and Iran are members, have yet to demonstrate their economic benefit.

16. (C) At the recent meeting of Iran-Russia Joint Economic Commission (see also ref A), the two sides agreed to create a special working group that would develop a "road map" for cooperative gas and oil projects. However, when we asked MFA Iran desk head Maxim Baranov on February 5 about this "road map," he simply replied that he "has read about it in the press as well," but has "yet to see it."

17. (SBU) On January 13, 2010, the Russian Energy Ministry hosted the first meeting of the Russia-Iran working group addressing cooperation on oil, gas, and petrochemicals. Following the meeting, Iran's Deputy Oil Minister, Hossein Noghrehkar Shirazi, stated that a plan for cooperation over the next thirty years would be developed.

NUCLEAR AND MILITARY SALES

18. (C) Another major area of "economic cooperation" is Russia's involvement in Iran's civilian nuclear energy and its sales of military equipment. Since 1995, Russia has been working on a contract to supply Iran with a reactor for the Bushehr power plant, completing work initiated by Germany in the 1970s. The Bushehr contract is currently valued at an estimated \$1 to \$1.5 billion over the life of the project.

However, fulfilling the contract may be important in terms of maintaining Russia's business reputation in the broader civilian nuclear sector. The GOR has also signed a contract to transfer the S-300 air defense missile system to Iran. While the monetary value of this deal is not large, estimated at up to \$800 million, it may also be important to maintaining and enhancing Russia's role as an arms supplier. To Iran's displeasure, however, both projects have faced delays.

¶9. (C) MFA officials tell us the contracts should not be linked and are delayed for different reasons. On the Bushehr contract, Baranov denied there were political motivations behind the delay, repeating previous claims that the delays were purely technical. The GOR, he argued, wanted to ensure the safety of the equipment and, therefore, needed more time for testing. While he expected Bushehr to come online sometime in 2010, he said there was no firm date scheduled. (Note: Baranov also told us that Russian Minister of Energy Sergey Shmatko is the leader of the Russian side of the Joint Economic Commission specifically because of his experience dealing with Iranian interlocutors from his previous job as head of Russia's Atomstroyexport, which manages Russia's export of civil nuclear technology. End note.)

¶10. (C) In contrast, Baranov hinted that delays in fulfilling the S-300 contract were not technical. While he refused to confirm that Iran had indeed made a down payment for the system, he reiterated the MFA's standard response that a decision to cancel the contract could only be made at the highest levels of the GOR.

AVIATION, TELECOMS, TRANSPORT, ELECTRICITY

MOSCOW 00000301 003 OF 004

¶11. (U) Economic developments in the aviation and telecommunications industries have thus far been modest. In August 2007, the Ilyushin Finance Company signed a \$200 million agreement with Iran's Air Tours Company to deliver five Tu-204-100 airplanes. In February 2008, the Russian United Aircraft Corporation (UAC) and the Iranian Aerospace Industries Organization signed a memorandum of intent on the initial purchase of Tu-204 and Tu-214 airplanes and subsequent licensed assembly of these two types of aircraft in Iran. The memorandum, according to UAC, concerns a period of ten years and one hundred aircraft, covered by a contract worth an estimated \$2.5 billion. However, independent experts are skeptical about the Iranian aviation industry's capacity to manage the assembly of airplanes on such a significant scale.

¶12. (U) In May 2008, MegaFon (one of the three largest mobile phone operators in Russia) opened a subsidiary in Iran and studied the possibility of participating in a tender for a license, which would give it rights to become a mobile operator in Iran. MegaFon had planned subsequent investments of up to \$4.5 billion. However, having reviewed the tender terms and other factors related to conducting business in Iran, the company refused to participate in the tender and stopped its work on the project.

¶13. (C) The MFA's Baranov told us that while there is interest on both sides to expand the economic relationship, concrete progress has not yet materialized. He said major proposed projects such as Russian participation in IPI gas pipeline and the development of a transportation corridor from Russia through Iran to India have not moved forward. He said the two sides did set up an entity to devise a plan to expand electricity trade, but that vast price differences for electricity in the two countries pose a major challenge. According to Baranov, the automobile sector is a potential bright spot in the relationship. He said Russia's Kamaz truck company is interested in expanding the number of models

it produces in its plant in Iran, and Iran hopes to expand production of spare parts used in Russian autos.

BANKING

¶14. (C) During his January visit to Moscow, Deputy Oil Minister Shirazi expressed confidence that Russia and Iran could use their national currencies for the implementation of joint energy projects. In addition, Russia and Iran reportedly plan to establish a joint bank to finance bilateral energy projects. Russia's Deputy Central Bank Governor Viktor Melnikov had reportedly planned to visit Tehran this month to work on mechanisms to conduct banking transactions in rubles. According to Baranov, however, the trip has been "postponed" and no new date has been set for the visit. (Note: We plan to raise this issue with Melnikov in an upcoming meeting. End note.)

¶15. (C) While Baranov stressed that expanded use of the ruble is a general Russian goal, he noted that it would be especially useful in doing business with Iran due to the "complications" of dollar transactions caused by U.S. sanctions. Baranov also admitted that the disparity in exports from Russia to Iran and imports from Iran makes the prospect of using national currencies in trade difficult (presumably as Russia would have to be willing to amass Iranian rials). He matter-of-factly added, "of course, Iran already has a bank in Russia, 'Bank Melli Iran Moscow,' that can conduct transactions in rubles, dollars, and euros."

COMMENT

¶16. (C) Even with political will, Russia-Iran economic ties as measured by trade and investment flows are unlikely to

MOSCOW 00000301 004 OF 004

become significant for Russia anytime soon. That said, given its role in the region, as a Caspian neighbor, and with its vast hydrocarbon resources, Iran is clearly of strategic importance for Moscow. That strategic significance, however, seems increasingly an issue of Russian interest in checking Iran's ambitions than of Iran as a valued economic partner. With its economy and government budgets highly dependent on oil and gas exports, Russia's medium-term economic interest would seem best served by high oil and gas prices with limited competition in those sectors. A stable Iran could challenge that interest, as expanded Iranian oil production would depress global oil prices, and increased Iranian gas production would compete directly with Russian gas for export markets. A more prosperous and less marginalized Iran would also compete with Russia for regional political influence.

¶17. (C) Furthermore, Russia currently enjoys literally billions of dollars in economic benefit from the oil price premium attributable to uncertainty surrounding Iran's future and the possibility of disruptions to oil shipments through the Straits of Hormuz. Should Iran engage in any military conflict, even a minor one, oil prices would likely rocket higher, providing Russia with even greater gains -- measured in the tens of billions of dollars -- from oil and gas exports.

¶18. (C) Although Baranov and others point out that Russia needs to be in Iran to compete with the Chinese and Indians, it is not clear what Russia gains in helping Iran develop its oil and gas resources -- the sectors in which it seeks to establish a presence. In the very long-term, a diversified Russian economy, with Russia-based international companies, would benefit from global reach, including in Iran. However, that future is very far off. End Comment.
Beyrle